DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 02-0478
Indiana Gross Retail and Use Tax
For 1999 and 2000

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ISSUE

I. Propane Tanks – Use Tax.

Authority: IC 6-2.5-5-8; Tri-States Double Cola Bottling Co. v Department of State Revenue, 706 N.E.2d 282 (Ind. Tax Ct. 1999); Department of State Revenue v. Indianapolis Transit System, 356 N.E.2d 1204 (Ind. Ct. App 1976); 45 IAC 2.2-5-15(b); Black's Law Dictionary (7th ed. 1999).

Taxpayer protests the proposed assessment of Indiana use tax on the purchase price of propane storage tanks which taxpayer later furnished its customers. Taxpayer maintains that the tanks are "leased" to its customers and that, as a result, the tanks are not subject to the use tax assessment.

STATEMENT OF FACTS

Taxpayer is an Indiana corporation in the business of supplying customers with propane (L.P.) gas. Taxpayer has a business location out of which a limited number of retail sales take place. However, the bulk of taxpayer's business consists of delivering gas to its customers.

During 2001 and 2002, the Department of Revenue (Department) conducted an audit review of taxpayer's business records and tax returns. As a result of that review, the Department concluded that taxpayer owed additional amounts of use tax. Taxpayer disagreed with a portion of the assessment and submitted a protest to that effect. An administrative hearing was conducted during which taxpayer explained the basis for its protest. This Letter of Findings results.

DISCUSSION

Taxpayer purchased propane tanks which it then provided to its customers. In purchasing the tanks, taxpayer did not pay sales tax. The audit determined that the tanks were not purchased for an exempt purpose and assessed use tax accordingly. The audit did so because it concluded that, although the customers paid to use the tanks, the tanks were not "leased" to taxpayer's customers. The audit listed the following reasons justifying the conclusion that the tanks were not leased.

1. The tanks were placed on the customers' property for the convenience of the taxpayer in order to make it possible for taxpayer to sell propane to those customers.

2. Taxpayer retained complete control over the tanks, and the customers could not – under the contract agreement or state law – purchase propane from another dealer.

3. Taxpayer retained the right to enter and leave that portion of the customers' property on which the tanks were located.

4. The parties' lease agreement stipulated that the tanks would remain taxpayer's personal property.

Taxpayer maintains that its initial purchase of the propane tanks was not subject to imposition of the Indiana gross retail (sales) tax. Although taxpayer does not specifically say as much, presumably taxpayer is claiming an exemption pursuant to IC 6-2.5-5-8 which states in part that, "Transactions involving tangible personal property are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of his business without changing the form of the property." The exemption provided for under IC 6-2.5-5-8 is amplified at 45 IAC 2.2-5-15(b) which provides, as a general rule, that "[s]ales of tangible personal property for resale, rental or leasing are exempt from tax if all of the following conditions are satisfied: (1) The tangible personal property is sold to a purchaser who purchases this property to resell, rent or lease it; (2) The purchaser is occupationally engaged in reselling, renting or leasing such property in the regular course of his business; and (3) The property is resold, rented or leased in the same form in which it was purchased."

The Indiana courts have provided guidance in determining whether a transaction between parties constitutes a lease agreement. In Department of State Revenue v. Indianapolis Transit System, 356 N.E.2d 1204 (Ind. Ct. App 1976), the court of appeals stated that "[w]hether certain circumstances created a lessor – lessee . . . relationship between the parties is a matter of fact dependent on possession of and control over the property involved." Id. at 1209. While finding that the Department's regulation did not contain a definition of "lease," the Tax Court in Tri-States Double Cola Bottling Co. v Department of State Revenue, 706 N.E.2d 282 (Ind. Tax Ct. 1999), concluded that a "lease" constituted the "transfer of a right to possession and use of goods for a term in return for consideration." Id. at 285.

Taxpayer enters into agreements with its customers to provide the customers with propane tanks. The agreements fall into essentially two categories; small tank agreements and large tank agreements. In implementing the small tank agreements, taxpayer purchased 120 gallons tanks which cost approximately $200 each. Taxpayer then furnished those tanks to its customers charging each customer $40 per year. Despite the terms of the parties' agreement, taxpayer apparently did not require that each small tank customer purchase a minimum amount of gas each year. Rather, the records demonstrate that a number of the small tank customers purchased a negligible amount of propane each year. Nonetheless, each small tank customer was charged $40 annually regardless of the amount of propane which the customer purchased that year.

Taxpayer also bought larger tanks which were furnished to certain of its customers. The large tank customers were charged a flat fee of $1 per year. However – unlike the small tank customers – the large tank customers paid a premium on the gas which was supplied to the customer. For example, during one pricing period, taxpayer charged its large tank customers $.66 for each gallon of propane delivered to those customers. In contrast, during the same pricing period, taxpayer charged $.55 for each gallon of propane that was delivered to a customer which did not use one of the taxpayer's large tanks. In those instances in which the lesser price was charged, the customer owned his own tank, did not need one of taxpayer's large tanks, and avoided the $.11 "premium" which the large tank customers paid. The $.11 price differential represented the amount that the large tank customer paid taxpayer for the privilege of using one of taxpayer's large tanks. In effect, each large tank customer paid $1.00 per year plus an additional premium based upon that customer's gas usage. Under the terms of the parties' agreement, each large tank customer was required to make a minimum yearly propane purchase "equal to two times the stated capacity of said tank as a minimum purchase requirement." Therefore, if a large tank customer obtained a 500 gallon tank, that large tank customer was required to purchase a minimum of 1,000 gallons of propane each year. If the customer failed to do so, taxpayer had the option of replacing the 500 gallon tank with smaller capacity tank.

Taxpayer's small and large tank customers signed the same "lease agreement" when the customers acquired one of taxpayer's propane tanks. That agreement requires that the customer purchase "his entire requirements of Propane gas form [taxpayer] and permit[] no other person, firm or corporation to store or fill said tank with propane or to service said equipment without [taxpayer's] prior written consent."

The customer is required to "permit [taxpayer] or its Authorized representative free and unlimited ingress, egress and access to and from [customer's] premises to deliver propane gas, service, inspect, or maintain said tank and equipment."

Under the terms of the agreement, the customer is not permitted to "remove said tank or equipment from [the customer's] premises." In addition, the tank "remain[s] the personal property of [taxpayer]."

Taxpayer's agreements with both the small and large tank customers do not constitute lease agreements because the customers do not come into "possession" of the tanks. "Possession" means the right to "exercise control over something to the exclusion of all others." Black's Law Dictionary 1183 (7th ed. 1999). By the terms of the agreement, the customer is not entitled to move the tanks or to allow another supplier to fill the tanks with the competitor's propane supply. Of course, the tanks are located on the customers' property, but that does not mean that the customers have "possession." Although the tank is located on the customer's property, taxpayer retains most of the rights to control the tank. Unlike an actual lease agreement, the customer does not acquire the usual rights to control the object of the lease. Instead the tanks are merely an extension of the agreement by which taxpayer provides propane to its customers with the customer assessed an additional cost for the use of the storage container which – by nature of the transaction – is necessarily located on the customer's property. The fact that the parties' agreement is called a "lease" does not change the fact that taxpayer is not in the business of leasing propane tanks nor the fact that the customers are not interested in leasing propane tanks.

Taxpayer's interest lies in selling its product to its customers and receiving compensation for the cost of doing so. The customers' interest is in obtaining that fuel. Given the fact that the tanks have a limited decorative or utilitarian value outside of their capability of storing taxpayer's propane, it is apparent that the object of the parties' agreement is the delivery, storage, and consumption of propane.

Neither the law nor the dictates of simple common sense allow a conclusion that taxpayer purchased the tanks in order to lease the tanks to its customers. Under IC 6-2.5-5-8, taxpayer is not "occupationally engaged" in the business of leasing storage tanks in the ordinary course of its business. Under 45 IAC 2.2-5-8(b), taxpayer is not "occupationally engaged" in renting propane tanks in the regular course of its business. Common sense dictates a finding that taxpayer is in the business of selling propane to customers who are interested in obtaining that fuel. The fact that the sale of propane necessarily involves the use of a storage container located on the customers' property does not alter the nature of the underlying transaction. Taxpayer is, of course, entitled to be fully compensated for the fact that it necessarily incurs expenses in delivering the propane to its customers. However, that compensation does not consist of lease payments.

FINDING

Taxpayer's protest is respectfully denied.

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